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Board of Directors
Fourteenth Annual Study
Banks & Other Financial Institutions
1987

KORN/FERRY INTERNATIONAL

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KORN/FERRY INTERNATIONAL
FOURTEENTH ANNUAL BOARD OF DIRECTORS STUDY OF BANKS AND OTHER FINANCIAL INSTITUTIONS

Introduction

For the past 14 years, Korn/Ferry International has surveyed 1,000 of America's leading corporations in an ongoing effort to collect information on the structure and function of the corporate board. As part of our annual study, we make a special analysis of the data pertaining to banks and other financial institutions.

This year, 532 companies responded to our survey, of which 83, or 16 percent, were financial institutions. As in the past two years, we found that discussions of board matters were once again dominated by two interrelated factors—concern over difficulties in recruiting and maintaining qualified directors and issues of liability.

The majority of financial respondents (67 percent) continue to believe that there is a problem finding and attracting qualified outside directors, and 79 percent state that the problem has not diminished since last year.

But despite this lingering problem, CEOs of financial institutions are more willing to take on additional directorships than their counterparts in other industries. Seventy percent of the chairmen of banks and financial institutions said that they would accept an additional board seat compared with only 55 percent of all the chairmen surveyed. And while, overall, 42 percent of our respondents reported having turned down a board seat in the past year, only 28 percent of financial respondents had done so, less than any other group. Furthermore, while respondents as a whole stated that a CEO should serve on no more than one or two boards, financial respondents believe that three or four board seats are appropriate.

Liability Crisis

The crisis of directors' liability insurance is still with us, and although 90 percent of banks and financial institutions have D&O insurance, seven percent were denied coverage within the last year.

Eighty-five percent of those with coverage saw their insurance premiums increase compared with 78 percent in 1985. And this year's increases were more dramatic—on average 462 percent (compared with 271 percent in 1985). Furthermore, 63 percent of the financial institutions experienced an average 42 percent decrease in total dollar coverage.

But most financial respondents feel that measures are in place to ease the crisis. Seventy-one percent said that the Delaware statute limiting director liability will at least partially rectify the situation. Perhaps the confidence of the banks is reflected in the fact that only 18 percent of them are concerned enough to ask shareholders to approve a measure limiting or eliminating director liability. Overall, 34 percent of our respondents were proposing such a measure to their shareholders.

Other Trends

While banks and financial institutions' boards decreased in size from an average 20 to 18 members, they are still the largest boards. Overall, company boards averaged only 13 directors.

Banks and financial institutions have taken the lead in the recruitment of women and minority directors. Forty-nine percent say they are actively seeking women and minority board members, as opposed to 28 percent overall. Currently, women sit on 61 percent of financial boards and members of ethnic minorities sit on 53 percent.

Despite pay boosts of six percent this year, financial directors still lag behind the average respondent in total compensation. They averaged $18,471, compared with an overall average compensation of $20,462.

These are some of the important trends that we found among banks and other financial institutions. A more detailed discussion follows in the Summary of Findings.

Lester B. Korn
Chairman

Richard M. Ferry
President

SUMMARY OF FINDINGS

On a question-by-question basis, the following findings relate directly to bank and other financial institution respondents (Table 1). Where appropriate, comparisons are made with all the participants in our study.*

1. Size of Board (Table 2)

Banks and other financial institutions have an average of 18 directors on their boards, compared with the average of 13 members for all responders and higher than any other group responding to this study. The average of 18 represents a decrease from the 20 members reported by banks and financial institutions last year.

2. Inside Directors vs. Outside Directors (Table 2)

Banks and other financial institutions also have the strongest preference for outside director dominance. Their boards average four inside and 14 outside directors, compared with three inside and 10 outside members for all companies.

3. Is the Chairman also the CEO? Is the CEO also the COO? (Table 3)

Banks and other financial institutions report that 83 percent of their chairmen also function as chief executive officers, compared with the overall average of 77 percent. They have among the lowest percentage of CEOs who are also the chief operating officers. Only 22 percent report that their CEO is also their COO, down from 30 percent in 1985 and compared with 38 percent for all respondents.

4. Board Composition (Table 4)

With their strong preference for outside representation, banks and other financial institutions rely most often on CEOs/COOs of other companies (79 percent) and retired executives of other companies (65 percent) for their outside directorships. (Senior executives of other companies declined to 58 percent from 84 percent in 1985 as a result of the addition of the new category "CEO/COO of other companies.") (Table 4A)

Women sit on 61 percent of all financial company boards, the same as last year and compared with 43 percent for all companies. Only insurance companies reported seating more women directors. Women board members are drawn primarily from the ranks of academia (Table 4B).

Banks and other financial institutions are also among the leaders in ethnic minority representation. Minorities sit on 53 percent of their boards, compared with the overall average of 30 percent and higher than their representation rate of 43 percent five years ago (Table 4A). Only retailers registered a higher percentage of minorities on their boards. As in 1985, financial companies draw

*This year, 532 corporations responded to our Annual Study. Industrial and service corporations account for 70 percent of the total, of which 194 companies have revenues in excess of $1 billion. Banks and other financial institutions account for 16 percent, insurance companies for 10 percent and retailers for five percent.

most of their minority members from the ranks of academia (35 percent) (Table 4B).

Other groups significantly represented on financial boards include retired or previously employed corporate officers (42 percent), attorneys who do not provide legal services for the company (47 percent, up from 33 percent last year) and former government officials (30 percent). Financial boards, however, continue to have a low percentage of investment bankers. Only five percent seat an investment banker, down from 10 percent in 1985 and compared with 24 percent for all respondents.

Thirty-six percent of banks and other financial institutions seat attorneys who provide legal services for the company, and 29 percent have major shareholders on the board, up from 18 percent in 1982 and 25 percent in 1985 (Table 4A).

Representation of academicians declined to 55 percent from 62 percent last year, as did commercial bankers, from 17 percent in 1982 and 1985 to 12 percent this year.

5. Committees (Table 5)

Ninety-nine percent of the financial respondents report having an audit committee. As in the past, the two other most prevalent committees are compensation/personnel and executive, cited by 91 percent and 87 percent, respectively, up from 85 and 78 percent, respectively, in 1985. Fifty-nine percent have a nominating committee, compared with the 58 percent reported by all respondents. Only 17 percent, however, report having a finance committee, the smallest percentage of all responding groups (Table 5A).

As in 1985, the executive and finance committees are the largest, with an average of seven members. The benefits committee is smallest, with only four members. The public affairs committee increased by one outside director, while the audit and benefits committees decreased by one outside director, back to the levels reported in 1984. While the finance committee increased by one inside director, respondents reported an average decrease by one outside director. The audit, compensation/personnel and benefits committees each are composed entirely of outside directors (Table 5B).

The finance committee meets most frequently, averaging 11 meetings, a substantial jump from the five meetings reported in 1985. Meetings of the executive committee continued to increase from a low of five reported in 1984 to nine meetings reported this year (Table 5C).

Forty-seven percent of the bank and other financial institution respondents believe that in order to improve productivity, there is a trend toward more committee-assigned tasks, compared with 38 percent of all respondents. Along with the executive committee, the compensation/personnel committee plays the predominant role in the management succession process (53 percent).

6. Compensation (Table 6)

The annual plus per-meeting fee method of compensation is still by far the most popular system of remunerating outside directors. Ninety-one percent of bank

and other financial institution respondents reported using this method, up from 84 percent five years ago. Five percent pay an annual fee only and four percent pay a per-meeting fee only.

Annual Plus Per-Meeting Fee (91 percent of the respondents)

The average total annual compensation for outside directors of banks and other financial institutions using this method of payment is $18,471, an increase of six percent over last year's average of $17,462 and 21 percent more than directors of financial companies earned five years ago ($15,310). Banks and other financial institutions still lag behind all other study respondents, by 10 percent, in total compensation.

The $18,471 total average compensation comprises an average annual fee of $11,313 and an average per-meeting fee of $669. Up two percent from last year, the upper quartile average for financial companies is $27,519, up from $26,938 last year but four percent lower than the $28,715 average for all respondents.

Annual Fee Only (Five percent of the respondents)

The average earnings of outside directors receiving an annual fee only climbed sharply to $19,350, 15 percent over the $16,840 reported by banks and other financial institutions last year, and 33 percent higher than the $14,600 reported five years ago. However, the average annual fee of $19,350 was slightly below the $19,744 average for all respondents.

Per-Meeting Fee Only (Four percent of the respondents)

The fee paid to outside directors of financial companies using this method of compensation averages $775, a 46 percent increase from five years ago, but a dip from last year's average per-meeting fee only of $800.

7. Committee Compensation (Table 7)

Eighty-seven percent of banks and other financial institutions compensate their directors additionally for serving on committees. While committee members generally receive a per-meeting fee, most chairmen are compensated with an annual fee (Table 7A).

Total Annual Compensation

Including committee fees, the average total compensation paid to outside directors of banks and other financial institutions was reported at $21,500, compared with $23,676 for all respondents.

The upper quartile average for directors of banks and other financial institutions was $33,168, compared with the overall average of $35,960 (Table 7B).

8. Additional Compensation Information (Table 8)

The highest paid outside director of a bank or financial institution receives an average $28,962 for all board services exclusive of any consulting arrangement, an increase of 40 percent over the $20,700 reported five years ago. The $28,962 average is also slightly higher than the overall average of $28,572.

The average upper quartile compensation for financial respondents is $48,706, compared with $46,665 for all respondents. The average upper quartile fee for banks and other financial institutions increased 26 percent over the 1985 average. Sixteen percent also pay at least one outside director additional consulting fees, up from 11 percent last year.

Thirty-eight percent of the financial respondents increased directors' compensation an average of $3,235 for their board members in 1986. This is 11 percent above the average increase for all respondents and 18 percent higher than the average increase of $2,732 for financial companies last year. Twenty-five percent predict an increase in board fees for the coming year, projecting an average increase of $2,329. Seventy-nine percent of the financial company respondents believe that their outside directors are adequately compensated, consistent with the response in 1985.

Fifty-seven percent of the banks and other financial institutions state that their board chairmen are primarily responsible for establishing board compensation. In 36 percent of the cases, the compensation/personnel committee is responsible, down from 44 percent in 1985. In 17 percent of the cases, the executive committee plays a role in establishing appropriate compensation.

Banks and other financial institutions continue to take the lead in allowing outside directors to defer board fees until after retirement. Eighty-three percent offered this option, considerably above the 67 percent for all respondents. In 1985, 76 percent of the financial institutions allowed their outside directors to defer fees and 63 percent did so five years ago. Twelve percent have a program that provides retirement benefits, slightly less than last year and less than any other respondent group.

Other benefits commonly offered include travel expense reimbursement (88 percent), directors' liability insurance (82 percent), accident insurance (34 percent) and matching educational gifts (34 percent).

Stock Ownership

Eighty-seven percent of the financial respondents stated that all directors should own some company stock, up from 81 percent last year. The average minimum number of shares indicated was 506.

Eighty-six percent of the financial respondents report that their outside directors do, in fact, own some stock in the companies they serve. Sixty-seven percent report having 11 or more outside directors who own stock, a greater number than any responding group.

Liability Insurance

Ninety percent of banks and other financial institutions have directors' liability insurance, although seven percent have been denied coverage within the past year. Eighty-five percent of the financial corporations responded that directors' liability insurance premiums were increased for those with policies up for renewal in 1986, up from 78 percent last year. Furthermore, the average premium increase jumped to 462 percent, compared with the average of 271 percent reported in 1985. Sixty-three percent experienced a decrease in total dollar

coverage, compared with the average 50 percent for all respondents. Coverage on average fell 42 percent, from $38 million to $22 million.

Thirty-seven percent of financial institutions are considering self-insurance, more than any other responding group. When asked if respondents had been approached to join a consortium, 83 percent of banks and other financial institutions reported in the affirmative, compared with the overall average of 52 percent. Fifty-nine percent would consider joining if asked, again, more than any other respondent group.

9. Board Practices and Policies (Table 9)

The boards of banks and other financial institutions averaged 10 regular meetings during the past year, two more than the average of eight for all respondents and up from nine meetings reported last year.

An outside director of a financial institution devoted an average of 107 hours to board-related business last year—less than the average of 114 for all respondents but greater than last year's average (99 hours) for financial companies. The upper quartile average for financial companies is 183 hours per year (Table 9A).

The chairmen of financial institutions spent considerable time on board-related activities, devoting 169 hours, the same as last year.

Based on reported compensation data, directors of financial companies received an hourly rate of $173, up 25 percent from the 1982 hourly rate of $138.

With committee fees taken into account, the average hourly rate for outside directors of banks and other financial institutions is $201, compared with $208 for all outside directors.

As in 1985, banks and other financial companies had more board resignations than any other reporting group. Forty-one percent reported the resignation of an outside director during the past year, well above the 29 percent figure for all companies. However, this figure was slightly less than last year's resignation rate for financial company respondents. Thirty-six percent cited time demands as the major reason for board resignations.

Fifty-nine percent added at least one new outside director. For the fourth consecutive year, banks more than any other group have added outside directors. (Four respondents reported that five or more outside directors were added to their boards in 1986.) Forty-five percent expect a board vacancy, again, more than any other respondents. Most banks and financial institutions continue to rely predominantly on recommendations by their chairmen and by other board members (each 80 percent) to identify and select new directors. Nevertheless, 66 percent reported some use of the nominating committee in selecting new directors, compared with the overall average of 58 percent (Table 9B). When asking a prospective director to sit on a board, 91 percent of the financial companies view broad management experience as the primary consideration, followed by personal stature (72 percent).

Twenty-four percent of financial institutions report that at least one prospective director declined an invitation to serve on their boards, the same as reported last year. Time commitment was the primary reason cited for declining such an invitation (Table 9C).

Ninety-two percent have a mandatory retirement age, compared with 77 percent for all respondents. The average retirement age is 68 for inside directors, 70 for outside directors and 69 for board chairmen.

The average age of the CEO is 58, and 59 for the respondents' outside directors. The average age of the youngest outside director is 48; the oldest, 69.

10. Issues (Table 10)

Financial results and strategic planning continue to be the two most important issues facing the boards of banks and other financial institutions. When asked to rank various board issues, 71 percent ranked financial results as the most significant issue. Ninety-six percent ranked it among the top three. Sixty-three percent ranked strategic planning either first, second or third. Other issues of significance were financing/capitalization (32 percent) and mergers/acquisitions (26 percent), followed by day-to-day operations (25 percent).

When asked to project rankings for the same issues five years from now, financial results again placed first, cited by 79 percent, up from 68 percent last year. Strategic planning was rated second in importance to financial results, cited by 58 percent. Financing/capitalization was cited by 25 percent of the financial population, followed by mergers/acquisitions, cited by 24 percent.

Eighty-two percent of the respondents spend the most board time on issues related to financial results. Thirty-eight percent are most occupied with strategic planning, followed by the issues of mergers/acquisitions and day-to-day operations (each 22 percent).

TABLE 1—PARTICIPATING COMPANIES

Eighty-three of America's major banks and financial institutions participated in our Fourteenth Annual Study.

Size (Assets)	Number of Financial Institutions	%
Under $10 billion	48	57.8%
$10 billion and over	35	42.2%
TOTAL	83	100.0%

Stock Exchange	Number of Financial Institutions	%
New York Stock Exchange	37	44.6%
American Stock Exchange	0	0.0%
Over-the-counter	35	42.2%
Other	11	13.2%
TOTAL	83	100.0%

TABLE 2—PRESENT NUMBER OF BOARD MEMBERS

What is the present number of board members?

Size of Financial Institution	Average Number Inside Directors	Average Number Outside Directors	Average Number Directors
Under $10 billion	3	13	17
$10 billion and over	4	16	20
Average	4	14	18

TABLE 3—CHAIRMAN ALSO CEO, CEO ALSO COO

Is the Chairman of the Board also the Chief Executive Officer?
Is the Chief Executive Officer also the Chief Operating Officer?

	Chairman/CEO %	CEO/COO %
Yes	82.9%	22.4%
No	14.5%	75.0%
No response	2.6%	2.6%
TOTAL	100.0%	100.0%

TABLE 4—BOARD COMPOSITION

4A. Are one or more of the following individuals on the board?

	1982 Financial Institutions	1986 Financial Institutions	1986 All Companies Surveyed
CEO/COO of other companies	—	78.9%	74.2%
Retired executive (other companies)	61.8%	64.5%	67.4%
Academician	57.9%	55.3%	49.7%
Senior executive (other companies)	96.1%	57.9%	46.0%
Woman	65.8%	60.5%	42.9%
Retired or previously employed corporate officer	47.4%	42.1%	40.2%
Attorney (does not provide legal services for the company)	38.2%	47.4%	35.3%
Major shareholder (not officer of the company)	18.4%	28.9%	30.9%
Ethnic minority member	43.3%	52.6%	29.5%
Former government official	32.9%	30.3%	27.6%
Commercial banker	17.1%	11.8%	25.0%
"Professional" director	15.8%	18.4%	25.0%
Investment banker	2.6%	5.3%	24.3%
Attorney (provides legal services for the company)	35.5%	35.5%	23.7%
Non-U.S. citizen	19.7%	14.5%	13.0%
International executive (American)	11.8%	7.9%	6.2%

FIVE YEAR TREND

4B. From which of the above functions are most women and ethnic minorities drawn?

Function	% Women	% Minorities
Academicians	37.0%	35.0%
Senior executives (other companies)	10.9%	17.5%
CEOs/COOs (other companies)	10.9%	25.0%
Former government officials	6.5%	0.0%
Attorneys (do not provide legal services)	4.3%	10.0%

TABLE 5—COMMITTEES

5A. Which of the following standing committees does the board have?

Committee	Financial Institutions	All Companies Surveyed
Audit	98.7%	97.5%
Compensation/Personnel	90.8%	90.5%
Executive	86.8%	80.4%
Nominating	59.2%	57.9%
Benefits	25.0%	25.0%
Finance	17.1%	34.6%
Public affairs	17.1%	9.9%
Corporate ethics	9.2%	7.2%

5B. What is the composition of each committee?

Committee	Average Number Inside Directors	Average Number Outside Directors	Average Number Directors
Audit	0	5	5
Compensation/Personnel	0	5	5
Executive	2	5	7
Nominating	1	4	5
Benefits	0	4	4
Finance	2	5	7
Public affairs	1	5	6
Corporate ethics	1	4	5

5C. How many committee meetings were held during the past 12 months?

Committee	1982 Average Number of Meetings	1985 Average Number of Meetings	1986 Average Number of Meetings
Audit	4	4	5
Compensation/Personnel	4	4	4
Executive	7	7	9
Nominating	2	2	2
Benefits	3	3	3
Finance	4	5	11
Public affairs	3	3	3
Corporate ethics	4	2	3

FIVE-YEAR TREND

TABLE 6—COMPENSATION

How are board members compensated?
Annual Plus Per-Meeting Fee (91 percent of respondents)

Annual Fee Amount	%
Under $5,000	7.6%
$5,000–$6,999	15.2%
$7,000–$10,999	24.2%
$11,000–$13,999	24.2%
$14,000 and over	28.8%
TOTAL	100.0%
Average Annual Fee	$11,313

PLUS

Amount Per Meeting	%
Under $250	—
$250–$499	16.9%
$500–$599	41.5%
$600–$799	26.2%
$800 and over	15.4%
TOTAL	100.0%
Average Per-Meeting Fee	$669

EQUALS

Total Annual Compensation	%
Under $7,000	1.5%
$7,000–$10,999	12.3%
$11,000–$13,999	10.8%
$14,000–$16,999	24.6%
$17,000–$19,999	9.2%
$20,000–$24,999	24.7%
$25,000 and over	16.9%
TOTAL	100.0%
Average Total Annual Compensation	$18,471

COMPENSATION (continued)

Annual Plus Per-Meeting Fee

Type and Size of Company	Average Compensation	Upper Quartile Average
Banks and other financial institutions	$18,471	$27,519
Insurance companies	$18,863	$26,530
Retailers	$22,249	$30,875
Service companies	$20,653	$28,542
Industrials		
Under $200 million	$14,207	$22,768
$200 million–$399 million	$15,560	$22,386
$400 million–$599 million	$17,011	$22,060
$600 million–$999 million	$20,593	$27,188
$1 billion–$2.999 billion	$21,279	$27,223
$3 billion–$4.999 billion	$26,447	$32,270
$5 billion and over	$28,820	$34,671
Average	$20,462	$28,715

TABLE 7—COMMITTEE COMPENSATION

7A. What is the average committee fee for outside directors?

Committee	Member	Chairman
	Average Per-Meeting Fee	Average Retainer
Audit	$511	$4,757
Compensation/Personnel	$512	$3,533
Executive	$532	$5,857
Nominating	$545	$2,453
Finance	$569	$6,000
Benefits	$427	$2,700

7B. What is the average total annual compensation, including committee fees, for outside directors?

Type and Size of Company	Average Compensation	Upper Quartile Average
Banks and other financial institutions	$21,500	$33,168
Insurance companies	$24,406	$38,073
Retailers	$25,999	$41,663
Service companies	$23,482	$34,907
Industrials		
Under $200 million	$15,290	$24,483
$200 million–$399 million	$17,110	$25,113
$400 million–$599 million	$19,700	$28,875
$600 million–$999 million	$22,414	$31,875
$1 billion–$2.999 billion	$25,146	$31,895
$3 billion–$4.999 billion	$31,399	$39,121
$5 billion and over	$36,548	$48,428
Average	$23,676	$35,960

TABLE 8—ADDITIONAL COMPENSATION INFORMATION

How much did the highest paid director receive in 1986 for all board services exclusive of any consulting arrangement?

Amount	%
Under $11,000	1.5%
$11,000–$16,999	14.7%
$17,000–$24,999	29.4%
$25,000–$29,999	14.7%
$30,000–$39,999	23.5%
$40,000 and over	16.2%
TOTAL	100.0%
Average	$28,962

Highest paid director

Type and Size of Company	Average Compensation	Upper Quartile Average
Banks and other financial institutions	$28,962	$48,706
Insurance companies	$30,756	$54,626
Retailers	$27,051	$46,080
Service companies	$27,890	$43,353
Industrials		
Under $200 million	$18,075	$27,639
$200 million–$399 million	$20,111	$31,534
$400 million–$599 million	$19,288	$26,900
$600 million–$999 million	$25,526	$38,211
$1 billion–$2,999 billion	$29,297	$41,511
$3 billion–$4,999 billion	$37,184	$50,677
$5 billion and over	$48,366	$81,151
Average	$28,572	$46,665

TABLE 9—BOARD PRACTICES AND POLICIES

9A. How many hours (estimated) do directors spend annually on board matters, including review and preparation time, meeting attendance and travel?

Number of Hours	%
Under 40	5.3%
40–70	17.1%
71–100	28.9%
101–130	18.4%
131–160	11.8%
161–190	2.6%
191 and over	6.7%
No response	9.2%
TOTAL	100.0%
Average	107 hours

Hours (continued)

Type and Size of Company	Number of Hours	Upper Quartile Average
Banks and other financial institutions	107	183
Insurance companies	134	296
Retailers	86	134
Service companies	108	197
Industrials		
Under $200 million	94	149
$200 million–$399 million	99	184
$400 million–$599 million	106	200
$600 million–$999 million	120	215
$1 billion–$2.999 billion	109	174
$3 billion–$4.999 billion	137	249
$5 billion and over	153	254
Average	114	204

9B. How are outside directors located for the board?

	% 1985	% 1986
Recommended by chairman	88.0%	80.3%
Recommended by board members	77.1%	80.3%
Nominating committee	65.1%	65.8%
Recommended by other corporate officers	43.4%	48.7%
Referred by executive acquaintances	8.4%	5.3%
Executive search	4.8%	2.6%

9C. Have any prospective directors declined an invitation to serve on the board during the past year?

	%
Yes	23.7%
No	75.0%
No Response	1.3%
TOTAL	100.0%

If yes, what are the predominant reasons?

	%
Time commitment	55.6%
Conflict of interest	27.8%
On too many boards	22.2%

TABLE 10—ISSUES

What is the relative importance of each of the following issues?

	% Ranking #1	% Ranking #1 or #2	% Ranking #1, #2 or #3
Financial results	71.1%	86.8%	96.1%
Strategic planning	6.6%	42.1%	63.2%
Financing/Capitalization	2.6%	11.8%	31.6%
Mergers/Acquisitions	3.9%	14.5%	26.3%
Day-to-day operations	6.6%	13.2%	25.0%
Management succession	5.3%	9.2%	14.5%
Industry competition	2.6%	9.2%	13.2%
Corporate takeovers	1.3%	7.9%	10.5%
Government relations	0.0%	1.3%	5.3%
Shareholder relations	0.0%	0.0%	3.9%
Communications/Public relations	0.0%	0.0%	2.6%
Environmental issues	0.0%	2.6%	2.6%

WORLDWIDE OFFICES

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